DRN-3446894

Financial Ombudsman Service

The complaint

Mr A complains about the advice given by Pi Financial Ltd (Pi), trading as Ingenious Pension Solutions, to transfer the benefits from his defined-benefit ('DB') occupational pension scheme to a personal pension. He says the advice was unsuitable for him and believes this has caused a financial loss.

What happened

Mr A says he was approached by Pi in 2018, he says this contact took place as a result of a 'cold call'. I understand Mr A was first contacted by a marketing agency that Pi used. But after this Mr A and Pi met to discuss his pension and retirement needs. I understand that Mr A was interested in releasing some tax-free cash from his pension. This was to renovate a property he owned overseas with a view to renting it out.

Pi completed a fact-finding process to gather information about Mr A's circumstances and objectives. This showed that:

- He was 58 years old and married. He had one dependent child who was aged 17. It was noted that Mr A expected his child to be dependent for another year.
- He was employed and earning around £33,000 a year. Mrs A was also employed
- He owned a property overseas and planned to renovate this and rent it out.
- He had deferred DB scheme benefits.
- And he currently contributed to his employers defined contribution (DC) occupational scheme which was worth approximately £40,000.

Pi also carried out an assessment of Mr A's attitude to risk, which it said was '5 of 10 or low medium'.

On March 2018, Pi advised Mr A to transfer his pension benefits into a personal pension and invest the proceeds. The suitability report said the reasons for this recommendation were that Mr A wanted to:

- Transfer the DB scheme into a personal pension to have flexibility when taking benefits and in retirement.
- Use the tax-free cash to finance an overseas property renovation with a view to renting it out.
- Retire from work at age 60 and perhaps live overseas for part of the year. But he didn't anticipate take an income from his pension until aged 65.

The transfer proceeded in the same month. Mr A transferred £111,848 into the personal pension. Shortly after the transfer Mr A took a tax-free cash withdrawal of £27,962.00. The personal pension was invested in one of the product providers lower risk managed portfolios.

Mr A complained in 2020 to Pi about the suitability of the transfer advice. He thought the advice was unsuitable for him and wasn't explained properly. And whilst there were some warnings about the transfer in the sale documentation, the general thrust of it was a very positive recommendation to transfer, despite the downsides to it.

Pi didn't uphold Mr A's complaint. It said Mr A was in an informed position about the transfer and it satisfied itself that he understood the advice. Pi said it gathered all the relevant information and it correctly advised Mr A to transfer. It thinks the complaint is frivolous.

Mr A referred his complaint to our service. An investigator upheld the complaint and recommended that Pi pay compensation. He thought that Mr A didn't have a high capacity, or tolerance, for risk, and he was likely to receive lower benefits due to the transfer. And his stated need to release some cash to renovate his overseas property wasn't a good reason for the transfer itself. And no other options to fund this were considered, such as borrowing or using some of Mr A's disposable income (as he was already). And the information about the rental property was very brief, it wasn't clear if this was a developed plan to provide an income.

Pi disagreed, saying that, in summary, if Mr A had used the tax-free cash to renovate his property he would have been in a position to retire at age 60. This is because of the rental income this property would have provided. So, whilst the transfer reduced his pension benefits it was still in his best interests to proceed with it.

I can see there was some further correspondence after the opinion, but no new issues were raised. And the Investigator wasn't persuaded to change their opinion. So, the complaint has been referred to me to make a final decision.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

I've taken into account relevant law and regulations, regulator's rules, guidance and standards and codes of practice, and what I consider to have been good industry practice at the time. This includes the Principles for Business ('PRIN') and the Conduct of Business Sourcebook ('COBS'). And where the evidence is incomplete, inconclusive or contradictory, I reach my conclusions on the balance of probabilities – that is, what I think is more likely than not to have happened based on the available evidence and the wider surrounding circumstances.

The applicable rules, regulations and requirements

The below is not a comprehensive list of the rules and regulations which applied at the time of the advice, but provides useful context for my assessment of Pi's actions here.

PRIN 6: *A firm must pay due regard to the interests of its customers and treat them fairly.*

PRIN 7: *A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.*

COBS 2.1.1R: *A firm must act honestly, fairly and professionally in accordance with the best interests of its client (the client's best interests rule).*

The provisions in COBS 9 which deal with the obligations when giving a personal recommendation and assessing suitability. And the provisions in COBS 19 which specifically relate to a DB pension transfer.

Having considered all of this and the evidence in this case, I've decided to uphold the complaint for largely the same reasons given by the investigator.

The regulator, the Financial Conduct Authority ('FCA'), states in COBS 19.1.6G that the starting assumption for a transfer from a DB scheme is that it is unsuitable. So, Pi should have only considered a transfer if it could clearly demonstrate that the transfer was in Mr A's best interests. And having looked at all the evidence available, I'm not satisfied it was in his best interests.

Financial viability

Pi carried out a transfer value analysis report (as required by the regulator) showing how much Mr A's pension fund would need to grow by each year in order to provide the same benefits as his DB scheme (the critical yield).

The advice was given after the regulator gave instructions in Final Guidance FG17/9 as to how businesses could calculate future 'discount rates' in loss assessments where a complaint about a past pension transfer was being upheld. Prior to October 2017 similar rates were published by the Financial Ombudsman Service on our website. Whilst businesses weren't required to refer to these rates when giving advice on pension transfers, they provide a useful indication of what growth rates would have been considered reasonably achievable for a typical investor.

Mr A was 58 at the time of the advice and wanted to retire at 65. The critical yield required to match Mr A's benefits at age 65 was 18.25% if he took a full pension and 11.65% if he took tax-free cash and a reduced pension.

The relevant discount rate closest to when the advice was given which I can refer to was published by the Financial Ombudsman Service for the period before 1 October 2017, was 2.6% per year for six years to retirement. I've kept in mind that the regulator's projection rates had also remained unchanged since 2014: the regulator's upper projection rate at the time was 8%, the middle projection rate 5%, and the lower projection rate 2%.

I've taken this into account, along with the composition of assets in the discount rate, Mr A's 'low to medium' attitude to risk and also the term to retirement. There would be little point in Mr A giving up the guarantees available to him through his DB scheme only to achieve, at best, the same level of benefits outside the scheme. But here, given the lowest critical yield was over 11%, I think Mr A was likely to receive benefits of a substantially lower overall value than the DB scheme at retirement, as a result of investing in line with that attitude to risk.

And this was recognised in the suitability letter when Pi said, referring to the critical yield, that it was *'a high and unrealistic return and will not be achievable, based on your risk profile and the term to retirement, you should be aware that there is no guarantee of future growth and it is possible that your eventual pension may be reduced by transferring.'*

Pi also gave an estimate of the funds required to purchase the annuity on the same basis as the DB scheme. If Mr A took all his benefits as pension he would need £298.969.09. If he took a reduced pension and some tax-free cash he would need £207,750.17. These are far in excess of what it is reasonable to expect Mr A's transferred out fund to grow to. And they give a revealing insight in to the value of the benefits he was giving up.

And Pi has provided cashflow models which it says show that Mr A would've been able to meet his needs despite the high critical yields. I've considered these. The model Pi reproduced in the suitability letter shows that if Mr A's fund grew at a 4.97%, which it said was reasonable for the fund he was to invest in, he would be able to withdraw on a similar rate form the DB scheme until his age 88, when the fund would be exhausted. Whilst this

was just beyond his life expectancy, if Mr A lived a longer life, or the fund performed poorly at times, there was a chance that Mr A's fund may run out.

Also, as Pi will know, past performance is no guarantee for future performance and so I consider the discount rates and the regulator's standard projections to be more realistic in this regard in the long term rather than projecting historic returns forward, particularly over such a long period of time.

For this reason alone a transfer out of the DB scheme wasn't in Mr A's best interests. Of course, financial viability isn't the only consideration when giving transfer advice, Pi has said that Mr A transferred as he had a need for tax-free cash and flexibility, and this need outweighed the financial disadvantages of the transfer. I've considered this below.

Flexibility and income needs

The main reason that this transfer was recommended was that Mr A wanted to access his pension fund and use the cash he could release to renovate a house he owned overseas. Pi has said that the predicted rental income, which was significant, would offset any loss in the guaranteed pension income Mr A would receive.

It's worth noting that Mr A did withdraw the maximum tax-free cash. But I understand less than half of this was used to start the property renovations. The remainder was spent on his family.

It was recorded that Mr and Mrs A wanted an income of £1,200 per month in retirement. Which is around £14,500 a year.

Mr A's DB scheme would have provided an increasing income of £7,092 per year if he took all of the benefits as a pension. Or he could have taken a lump sum of £28,368 and a pension of £4,255. He was also a member of his current employers DC scheme and he'd built up a fund of £40,000 so far. Both him and his employer were contributing 14% of his salary into this. It's not recorded on the fact find, but I assume that Mr A would also receive some state pension provision.

There is no record of any provision Mrs A may have had, in fact other than her name there is very little detail about her at all in the time of sale documentation. I think this is a serious failing. I can't see how Pi could have given M A proper advice on his retirement if it wasn't aware of what Mrs A would be entitled to.

So, it's not certain, but it seems reasonable to say that Mr A's existing provision could provide the income he says he wanted. In summary he would get his is £7,000 a year from his DB scheme. Some state provision which can be around £9,000, and what his DC scheme would provide in six years time. So, I think it's likely he had provision for what he wanted at retirement. Or very close to it.

But Mr A couldn't take the benefits flexibly from the DB scheme. He had to take both the tax-free cash and the pension at the same time. And, as I've outlined above, if Mr A retired early, or took tax-free cash then the amount of income he'd get would be lower. Although this isn't a penalty it's to reflect either the amount taken as cash, or the longer time the pension would be in payment. I don't think Pi was providing clear fair and not misleading information when it said the reduction for early retirement was a penalty.

So, what I've got to consider here is was the proposed property development a good enough reason for Mr A to give up his guaranteed pension income. This needs to be considered in the context that the transfer would almost certainly reduce Mr A's income from his pension.

And the regulations are clear in that this was likely to be unsuitable. For this reason, it needs to be shown, in some detail, that the rental property benefits were very likely, or even certain to, outweigh the benefits he was giving up.

It's not reasonable to recommend a transfer when it is just a 'nice to have' or a 'good idea'. And even if it was established that the rental property was a good way forward for Mr A, it also needs be established that he couldn't have funded the house renovations another way.

It's clear that Mr A thought his property would provide a significant income when it was renovated. But there was no detailed analysis of this at the time of sale. There was no information how Mr A derived the estimated income and no consideration of any costs he would expect to pay, such as ongoing maintenance.

Pi has essentially said that it looked at photographs of the property which looked impressive. And it was made aware that it was in a tourist area. So, it should be able to provide a decent income. But I don't think there is anywhere near enough information here for it to be able to say that Mr A should have given up his guaranteed pension income to fund this.

And there was also no consideration about how Mr A could have funded this any other way. It was noted he was spending his spare income on the property each month. So, it's not clear why this spare income, which was around £800 a month, could not have been the basis, for example, to fund some borrowing. Again, this really needed to be explored before Pi could give advice on the DB transfer.

I appreciate that this may have gone beyond what Pi could be reasonably expected to do, but if this was the case it should have said so, and not advised Mr A to transfer.

Overall, I don't think Mr A required flexibility in retirement. This is because, based on the evidence I've seen, I don't think he had a genuine need to access his tax-free cash earlier than the normal scheme retirement age and leave his funds invested until a later date. I also can't see evidence that Mr A had a strong need for variable income throughout retirement. This doesn't seem to have been discussed

I'm satisfied Mr A could have better met his income needs in retirement through the DB scheme at age 65. I think the guaranteed income would have been valuable to him and could have formed a core of his retirement income. I don't think his plans to rent his overseas property represented a good enough reason to transfer his DB scheme benefits.

Death benefits

It was documented at the time of sale that Mr A preferred the death benefits of a personal pension. Although I don't think a genuine needed was established, again it was more of a 'nice to have.'

That said, death benefits are an emotive subject and of course when asked, most people would like their loved ones to be taken care of when they die. The lump sum death benefits on offer through a personal pension were likely an attractive feature to Mr A. But whilst I appreciate death benefits are important to consumers, and Mr A might have thought it was a good idea to transfer his DB scheme to a personal pension because of this, the priority here was to advise Mr A about what was best for his retirement provisions. A pension is primarily designed to provide income in retirement. And I don't think Pi explored to what extent Mr A was prepared to accept a lower retirement income in exchange for higher death benefits.

I also think the existing death benefits attached to the DB scheme were underplayed. Mr A was married (he had children but they were very soon to be non dependent) and so the spouse's pension provided by the DB scheme would've been useful to his wife if Mr A predeceased her. I don't think Pi made the value of this benefit clear enough to Mr A. This was guaranteed and it escalated – it was not dependent on investment performance, whereas the sum remaining on death in a personal pension was. And as the cashflow analysis shows, there may not have been a large sum left particularly if Mr A lived a long life. In any event, Pi should not have encouraged Mr A to prioritise the potential for higher death benefits through a personal pension over his security in retirement.

Furthermore, if Mr A genuinely wanted to leave a legacy for his wife and children, which didn't depend on investment returns or how much of his pension fund remained on his death, I think Pi should've instead explored life insurance.

Overall, I don't think different death benefits available through a transfer to a personal pension justified the likely decrease of retirement benefits for Mr A. And I don't think that insurance was properly explored as an alternative.

Control or concerns over financial stability of the DB scheme

I think Mr A's desire for control over his pension benefits was overstated. Mr A was not an experienced investor, and I cannot see that he had an interest in or the knowledge to be able to manage his pension funds on his own. So, I don't think that this was a genuine objective for Mr A – it was simply a consequence of transferring away from his DB scheme.

I can see that the scheme was underfunded and this was considered at the time of sale. I can't see that transfer was recommended for this reason though. And it was also noted that the employer was making 'catch up' payments and the underfunding would be resolved in the future. So, the funding of his employer's DB scheme was not in a position such that Mr A should have genuinely been concerned about the security of his pension – if he was.

Suitability of investments

Pi recommended that Mr A invest in a number of funds. As I'm upholding the complaint on the grounds that a transfer out of the DB scheme wasn't suitable for Mr A, it follows that I don't need to consider the suitability of the investment recommendation. This is because Mr A should have been advised to remain in the DB scheme and so the investments in these funds wouldn't have arisen if suitable advice had been given.

Summary

I don't doubt that the ready access to some cash, flexibility, control and potential for higher death benefits on offer through a personal pension would have sounded like attractive features to Mr A. But Pi wasn't there to just transact what Mr A might have thought he wanted. The adviser's role was to really understand what Mr A needed and recommend what was in his best interests.

Ultimately, I don't think the advice given to Mr A was suitable. He was giving up a guaranteed, risk-free and increasing income. By transferring, Mr A was very likely to obtain lower retirement benefits and in my view, there were no other particular reasons which would justify a transfer and outweigh this. Mr A shouldn't have been advised to transfer out of the scheme just to try and pay for the renovations to his overseas property and the potential for higher death benefits wasn't worth giving up the guarantees associated with his DB scheme.

So, I think Pi should've advised Mr A to remain in his DB scheme.

Of course, I have to consider whether Mr A would've gone ahead anyway, against Pi's advice.

I've considered this carefully, but I'm not persuaded that Mr A would've insisted on transferring out of the DB scheme, against Pi's advice. I say this because Mr A was an inexperienced investor with a low to moderate attitude to risk and this pension accounted for the majority of Mr A's retirement provision. So, if Pi had provided him with clear advice against transferring out of the DB scheme, explaining why it wasn't in his best interests, I think he would've accepted that advice.

I'm not persuaded that Mr A's need to fund his rental property were so great that he would've insisted on the transfer knowing that a professional adviser, whose expertise he had sought out and was paying for, didn't think it was suitable for him or in his best interests. If Pi had explained that Mr A could meet all of his objectives without risking his guaranteed pension, I think that would've carried significant weight. So, I don't think Mr A would have insisted on transferring out of the DB scheme.

In light of the above, I think Pi should compensate Mr A for the unsuitable advice, using the regulator's defined benefits pension transfer redress methodology.

Putting things right

On 2 August 2022, the FCA launched a consultation on new DB transfer redress guidance and set out its proposals in a consultation document - https://www.fca.org.uk/publication/consultation/cp22-15.pdf

In this consultation, the FCA said that it considers that the current redress methodology in Finalised Guidance (FG) 17/9 (Guidance for firms on how to calculate redress for unsuitable defined benefit pension transfers) remains appropriate and fundamental changes are not necessary. However, its review has identified some areas where the FCA considers it could improve or clarify the methodology to ensure it continues to provide appropriate redress.

A policy statement was published on 28 November 2022 which set out the new rules and guidance-https://www.fca.org.uk/publication/policy/ps22-13.pdf. The new rules will come into effect on 1 April 2023.

The FCA has said that it expects firms to continue to calculate and offer compensation to their customers using the existing guidance in FG 17/9 for the time being. But until changes take effect firms should give customers the option of waiting for their compensation to be calculated in line with the new rules and guidance.

We've previously asked Mr A whether he preferred any redress to be calculated now in line with current guidance or wait for the new guidance/rules to come into effect. He didn't make a choice, so as set out previously I've assumed in this case he doesn't want to wait for the new guidance to come into effect.

I am satisfied that a calculation in line with FG17/9 remains appropriate and, if a loss is identified, will provide fair redress for Mr A.

A fair and reasonable outcome would be for the business to put Mr A, as far as possible, into the position he would now be in but for Pi's unsuitable advice. I consider Mr A would have most likely remained in his DB scheme if suitable advice had been given.

Pi must therefore undertake a redress calculation in line with the regulator's pension review guidance as updated by the Financial Conduct Authority in its Finalised Guidance 17/9: Guidance for firms on how to calculate redress for unsuitable DB pension transfers.

For clarity, Mr A has not yet retired, and he has no plans to do so at present. So, compensation should be based on his normal retirement age of 65, as per the usual assumptions in the FCA's guidance.

This calculation should be carried out as at the date of my final decision and using the most recent financial assumptions at the date of that decision. In accordance with the regulator's expectations, this should be undertaken or submitted to an appropriate provider promptly following receipt of notification of Mr A's acceptance of the decision.

Pi may wish to contact the Department for Work and Pensions (DWP) to obtain Mr A's contribution history to the State Earnings Related Pension Scheme (SERPS or S2P). These details should then be used to include a 'SERPS adjustment' in the calculation, which will take into account the impact of leaving the occupational scheme on Mr A's SERPS/S2P entitlement.

If the redress calculation demonstrates a loss, the compensation should if possible be paid into Mr A's pension plan. The payment should allow for the effect of charges and any available tax relief. The compensation shouldn't be paid into the pension plan if it would conflict with any existing protection or allowance.

If a payment into the pension isn't possible or has protection or allowance implications, it should be paid directly to Mr A as a lump sum after making a notional deduction to allow for income tax that would otherwise have been paid. Typically, 25% of the loss could have been taken as tax-free cash and 75% would have been taxed according to his likely income tax rate in retirement - presumed to be 20%. So, making a notional deduction of 15% overall from the loss adequately reflects this.

The payment resulting from all the steps above is the 'compensation amount'. This amount must where possible be paid to Mr A within 90 days of the date Pi receives notification of his acceptance of my final decision. Further interest must be added to the compensation amount at the rate of 8% per year simple from the date of my final decision to the date of settlement for any time, in excess of 90 days, that it takes Pi to pay Mr A.

It's possible that data gathering for a SERPS adjustment may mean that the actual time taken to settle goes beyond the 90 day period allowed for settlement above - and so any period of time where the only outstanding item required to undertake the calculation is data from DWP may be added to the 90 day period in which interest won't apply.

If the complaint hasn't been settled in full and final settlement by the time any new guidance or rules come into effect, I'd expect to carry out a calculation in line with the updated rules and/or guidance in any event.

Where I uphold a complaint, I can award fair compensation of up to £160,000, plus any interest and/or costs that I consider are appropriate. Where I consider that fair compensation requires payment of an amount that might exceed £160,000, I may recommend that the business pays the balance.

My final decision

Determination and money award: I uphold this complaint and require Pi Financial Ltd to pay Mr A the compensation amount as set out in the steps above, up to a maximum of £160,000.

Where the compensation amount does not exceed £160,000, I would additionally require Pi Financial Ltd to pay Mr A any interest on that amount in full, as set out above.

Where the compensation amount already exceeds £160,000, I would only require Pi Financial Ltd to pay Mr A any interest as set out above on the sum of £160,000.

Recommendation: If the compensation amount exceeds £160,000, I also recommend that Pi Financial Ltd pays Mr A the balance. I would additionally recommend any interest calculated as set out above on this balance to be paid to Mr A.

If Mr A accepts this decision, the money award becomes binding on Pi Financial Ltd.

My recommendation would not be binding. Further, it's unlikely that Mr A can accept my decision and go to court to ask for the balance. Mr A may want to consider getting independent legal advice before deciding whether to accept any final decision.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr A to accept or reject my decision before 10 March 2023.

Andy Burlinson
Ombudsman